

REPORT OF THE AUDITOR-GENERAL TO THE MEMBERS OF THE COUNCIL ON THE FINANCIAL STATEMENTS OF THE NALEDI LOCAL MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2006

1. AUDIT ASSIGNMENT

The financial statements as set out on pages ... to ..., for the year ended 30 June 2006, have been audited in terms of section 188 of the Constitution of the Republic of South Africa, 1996, read with sections 4 and 20 of the Public Audit Act, 2004 (Act No. 25 of 2004) and section 126 of the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA). These financial statements are the responsibility of the Municipal Manager. My responsibility is to express an opinion on these financial statements, based on the audit.

2. NATURE AND SCOPE

The audit was conducted in accordance with the International Standards on Auditing read with General Notice 1512 of 2006, issued in Government Gazette no. 29326 of 27 October 2006. Those standards require that I plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement.

An audit includes:

- examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements
- assessing the accounting principles used and significant estimates made by management
- evaluating the overall financial statement presentation.

Furthermore, an audit includes an examination, on a test basis, of evidence supporting compliance in all material respects with the relevant laws and regulations which came to my attention and are applicable to financial matters.

I believe that the audit provides a reasonable basis for my opinion.

3. BASIS OF ACCOUNTING

The municipality's policy is to prepare the financial statements on the entity specific basis of accounting as described in paragraph 1.1 of the accounting policies to the financial statements.

4. QUALIFICATION

4.1 Opening balances

The audit opinion for the 2004/2005 financial year was disclaimed. During the year under review corrective measures were only implemented towards the end of the financial year and no adjustments were made on qualifications reported in the prior year. The unadjusted errors amounted to R46 282 284.

As a result I was unable to verify the opening balances other than agreeing them to the prior year financial statements.

4.2 Long-term liabilities and short-term portion of long-term liabilities

4.3.1 Confirmations for loans amounting to R4 991 764 could not be obtained and amortisation schedules could not be provided for auditing.

4.3.2 Short-term portions of long-term loans with an original balance of R2 533 157 did not form part of the amount that was transferred to current liabilities and no amortisation schedules for these loans could be provided.

As a result I could not verify the above-mentioned loans that are included in long-term liabilities with a balance of R27 689 771 and the short-term portion of long term liabilities with a balance of R2 005 472 as disclosed in the financial statements.

4.3 Consumer deposits

4.4.1 The balance for consumer deposits differs from the consumer deposit list provided by an amount of R352 149 and no reconciliation was performed between the consumer deposit list and the general ledger.

4.4.2 No supporting documentation or listing could be provided for guarantees in lieu of electricity and water deposits amounting to R270 430 as disclosed in note 5 to the financial statements.

4.4 Fixed Assets

No fixed asset register could be provided for auditing and no asset count was performed at year-end. In the absence of these documents alternative procedures could not be performed.

As a result I could not verify the fixed asset balance amounting to R44 200 254 as disclosed in the financial statements.

4.5 Investments

Reconciliations between the investment accounts and the general ledger were not performed. Confirmations obtained from third parties do not reflect the investment balances at year-end as disclosed in the financial statements.

As a result I could not verify the investment balance amounting to R2 941 840 as disclosed in the financial statements.

4.6 Long-term debtors and short-term portion of long-term debtors

Included in long-term debtors are uncleared and unreconciled suspense accounts with credit balances amounting to R498 142 and debit balances amounting to R276 752. The short-term portion of long-term debtors with a balance of R14 910 could not be verified due to the fact that supporting documentation, listing, debtors list, reconciliation and calculation of the short-term portion could not be provided for auditing.

4.7 Inventory

4.8.1 The inventory balance as per the financial statements remained unchanged from the prior year, a stock count was not performed, stock reconciliation was not performed, stock listing or inventory register could not be provided for auditing and inventory in the financial statements was not classified according to the appropriate categories as required by the Institute of Municipal Finance Officers (IMFO).

4.8.2 The inventory for game held at Leon Taljaard Game Reserve was not counted and valued at year-end (prior year R2 407 250) and it was not disclosed as part of inventory in the financial statements.

As a result, I could not verify inventory amounting to R2 667 291 as disclosed in the financial statements.

4.8 Debtors

4.8.1 The debtor's age analysis provided for auditing differ from the debtors balance as disclosed in the financial statements. No reconciliation or explanation could be provided for the difference amounting to R7 380 711.

4.8.2 Included in the debtors balance are uncleared and unreconciled debtors suspense accounts amounting to R7 791 565.

4.8.3 A register of indigent debtors could not be provided for auditing and I could therefore not determine the collectability of the debtors disclosed. The extent of free basic services could therefore also not be confirmed.

4.8.4 A calculation for the provision for bad debts amounting to R7 761 127 could not be provided. Debtors amounting to R29 571 215 were written off in the subsequent financial year.

As a result, I could not verify debtors amounting to R70 706 030 as well as the provision for bad debts amounting to R7 761 127 as disclosed in the financial statements.

4.9 Bank and cash

4.9.1 Stale cheques older than six months amounting to R8 994 817 and dishonored cheques amounting to R165 801 were not written back at the end of the financial year.

Payments received from debtors amounting to R6 286 899 were not posted to the cashbook and debtor accounts. Cheques amounting to R636 990 received from debtors which were dishonoured by the bank, were not written back in the accounting records.

4.10 Provisions

No provision was made for leave gratuity in the financial year and the balance disclosed only represents the remainder of the prior year's provision, resulting in a possible material understatement (prior year R940 000). Due to an insufficient leave records system alternative procedures could not be performed.

4.11 Creditors

4.11.1 A creditors list and supporting documents could not be provided for creditors amounting to R8 533 326 and creditors reconciliations were not performed during the year and at year-end.

4.11.2 Included in the creditors balance are uncleared and unreconciled creditors suspense accounts amounting to R10 573 522.

4.11.3 Supporting documentation and reconciliations for the value-added tax creditor amounting to R10 665 527 could not be provided.

As a result I could not verify the creditors amounting to R28 661 763 as disclosed in the financial statements.

4.12 Revenue

4.12.1 Grants received as disclosed in the financial statements differed from the confirmations received from third parties by R625 298. No alternative procedures could be performed.

4.12.2 The confirmations received for the Municipal Infrastructure Grants indicated an understatement of grants received amounting to R3 185 588.

4.12.3 The valuation roll was not properly maintained and updated with recent property valuations and additions, resulting in a significant loss of revenue.

1.12.4 Interest was not charged on outstanding debtors resulting in a significant loss of revenue due to the high value of outstanding debtors.

As a result, I could not verify revenue amounting to R90 164 520 as disclosed in the financial statements.

4.13 Expenditure

Expenditure amounting to R47 145 296 could not be verified due to insufficient supporting documentation.

4.14 Employee cost

A payroll reconciliation or explanation could not be provided for the difference of R1 300 072 between the total employee cost as per the financial statements and the payroll register.

4.15 Contingent liabilities

4.15.1 Legal claims against the municipality and the municipal manager amounting to R5 876 989 were not disclosed as required by IMFO.

4.15.2 Bond guarantees issued by the municipality on behalf of employees amounting to R668 030 could not be verified as listings and reconciliations could not be provided for auditing.

4.15.3 The last actuarial valuation of retirement benefits was done in 2001 and supporting documents could not be provided for audit to determine the current position of the pension fund and any possible liability on the part of the municipality.

4.16 Capital commitments

A list of capital commitments could not be provided for auditing. Audit work performed revealed that capital projects amounting to R245 968 were not included in the capital commitments note to the financial statements.

4.17 Non-routine journals

Supporting documentation could not be provided for non-routine journals amounting to R17 381 123. Audit tests revealed that there was no segregation of duties in the preparation, posting, reviewing and authorisation of these journals.

4.18 Cash flow statement

Audit work performed revealed material calculation errors in the cash flow statement amounting to R5 921 970.

4.19 Going concern

Given the uncertainty regarding the recoverability of debtors mentioned in paragraph 4.9 and the fact that:

- Funds amounting to R27 013 272 are not represented by cash or investments;
- Value-added-tax was not timeously paid over to the South African Revenue Service;
- Loans could not be repaid in accordance with the conditions of the loans;
- Material outstanding cheques amounting to R12 548 567 were not released to the beneficiaries after year-end, and
- The bank overdraft amounts to R 22 112 330,

future liquidity constraints may result in the municipality being unable to realise its assets and discharge its liabilities in the normal course of business. This casts serious doubt on the municipality's ability to continue as a going concern. Management did not make a proper assessment nor was the going concern assumption disclosed in the financial statements.

As a result, I could not to obtain reasonable assurance as to the municipality's ability to continue as a going concern in the foreseeable future.

5. DISCLAIMER OF AUDIT OPINION

Because of the significance of the matters referred to in paragraph 4, I do not express an opinion on the financial statements.

6. EMPHASIS OF MATTER

Without further qualifying the audit opinion, attention is drawn to the following matters:

6.1 Financial statement disclosures

The financial statements of the municipality do not comply with the disclosure requirements of IMFO and the MFMA in respect of the following:

- The electricity reticulation losses as disclosed in Annexure F differ with our recalculation by R504 149.
- The cash flow statement references external cash investment to note 20 of the notes to the financial statement instead of note 23.
- Note 28 relating to grants received amounting to R15 889 297 could not be reconciled with the grants received as per the Income Statement.

6.2 Non-compliance with laws and regulations

6.2.1 The following instances of non-compliance with the MFMA were noted:

- The accounting officer did not take all reasonable steps to ensure that full and proper records of the financial affairs of the municipality are kept in accordance with any prescribed norms and standards.
- The accounting officer failed to submit the budget statement after the end of each month to the mayor of the municipality and the relevant provincial treasury.
- The municipality failed to take all reasonable steps to ensure that proper mechanisms and separation of duties in the supply chain management system are in place to minimise the likelihood of fraud, corruption, favouritism and unfair and irregular practices.

6.2.2 Internal control and other matters

- Insufficient segregation of duties within the finance department was due to vacant posts.
- Investment, asset and inventory management policies do not exist.
- Applications for new connections are not screened, reviewed and approved by a senior official.

6.3 Computer Information Systems review

Proper Information Technology (IT) governance structures were not in place which includes policies and procedures, defined IT processes, proper IT strategic plan and staffing to support and properly monitor the IT functions.

7. APPRECIATION

The assistance rendered by the staff of the Naledi Local Municipality during the audit is sincerely appreciated.

AJ Grobler for Auditor-General

Rustenburg

30/11/2006



A U D I T O R - G E N E R A L